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Statement on the revision of the two European Block Exemption Regulations ("BERs") for horizontal cooperation agreements, Commission Regulation (EU) No 1217/2010 on the application of Art 101 (3) TFEU to certain categories of research and development agreements and Commission Regulation (EU) No 1218/2010 on the application of Art 101 (3) TFEU to certain categories of specialisation agreements (together "Horizontal BERs"), as well as the Commission's Guidelines on the application of Art 101 TFEU to horizontal co-operation agreements (2011/C 11 – "Horizontal Guidelines")

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The German Federal Bar (Bundesrechtsanwaltskammer, BRAK) is the umbrella organisation of the self-regulatory bodies of the German *Rechtsanwälte*. It represents the interests of the 28 German Bars and thus of the entire legal profession in the Federal Republic of Germany, which currently consists of approximately 166,000 lawyers, vis-à-vis authorities, courts and organisations at national, European and international level.

Opinion

This statement provides comments on the new Draft Horizontal Guidelines and the Draft BERs dated March 1, 2022. BRAK's comments will focus on **R&D agreements** (below 2.), and **standard development in an IPR context** (below 3.)

1. Previous Contributions in the Horizontal Reform Process

BRAK has provided comments in the course of the previous consultations regarding the reform of the Horizontal BERs and Horizontal Guidelines since 2019.

2. R&D Agreements

Following BRAK's comments to the R&D BER and the related guidance on R&D agreements more generally in the Horizontal Guidelines in February 2020 BRAK would like to now limit its comments on two important aspects regarding the Draft R&D BER and the related passages in the Draft Horizontal Guidelines.

2.1 Duration of Exemption under the Draft R&D BER

Limiting the exemption under the R&D BER in cases of joint exploitation to 7 years from the time the contract products/technologies are first put on the market within the EU ("7-years-period", Art 7(4) Draft R&D BER), is not reconcilable with the significant upfront investments associated with R&D efforts in industries with long R&D and product life cycles and continued IP protection for research results, for example in the pharmaceutical industry. BRAK has commented on the 7-years-period already in its initial submission of February 2020 but in view of the Draft R&D BER the Commission does not plan any changes in this regard.

As a result of the 7-years-period, the group exemption does not provide the intended safe harbour for many R&D agreements in various industries and, consequently, in BRAK's view, one important goal pursued by the Commission with providing a safe harbour under the R&D BER, i.e. to foster and stimulate even more innovation through highly needed R&D cooperation, is not achieved or at least unduly hampered.

The 7-years-period is particularly important in practice, given that in the majority of all joint R&D agreements, regardless of the industry, the parties will jointly exploit the R&D results within the meaning of Art 1(1) no. 13 Draft R&D BER, regularly by way of specialization between them (Art 1(1) no. 14 Draft R&D BER).

Due to the fact that the R&D and product life cycle (and associated IP protection) following completion of the joint R&D tends to be longer than the 7 years, the parties effectively need to provide for provisions in their R&D agreement for this future time period, given that there is practically no way for them to predict their market shares with any certainty after 7 years and, consequently, if they are able to continue profiting from the group exemption within the market share threshold of 25% (cf. Art 6(5) Draft R&D BER). This is particularly burdensome for non-competing parties to R&D agreements for which according to the other provisions of the Draft R&D BER the market share threshold is only meant to become relevant after this 7-years-period (cf. Art 6(1) Draft R&D BER) and not at the time of entering into the R&D agreement.

In practice, to be on the safe side, the contract parties that jointly exploit the R&D results by way of specialization (e.g. production and distribution) will need to agree already at the time of entering into the R&D agreement that after the 7-years-period they will grant each other unlimited access to the R&D results in order not to lose the benefit of the block exemption (cf. Art 3(4), 3(1) Draft R&D BER). Bearing in mind the typically limited risk of anticompetitive effects of cooperation agreements between non-competitors this de facto obligation for such (non-competing) R&D partners is particularly strict. In practice, it reduces any given party's willingness to enter into joint R&D agreements altogether, an outcome resulting from the provisions of the Draft R&D BER (and the current R&D BER) which is contrary to the Commission's goal to promote and stimulate innovation through cooperation in the R&D field.

In view of these considerations, BRAK suggests to extend the exemption duration from 7 years to at least 10 years from first putting the contract products/technologies on the market within the EU, this extension would not only provide more legal certainty for R&D investing companies but also avoid the burden of undue complexities in the R&D agreements.

2.2 Application of the Concept of Competition in Innovation

The Commission has now included the concept of innovation competition by virtue of "undertaking competing in innovation" in the Draft R&D BER (Art 1(1) no. 18 and no. 19), providing it with a new meaning - and new assessment parameters - by introducing the notion of "competing R&D efforts" (Art 1(1) no. 19 Draft R&D BER).

In sum, BRAK considers this concept as currently set out in the Draft R&D BER very difficult to be applied in practice. It will largely add to the complexity of assessing as to whether R&D agreements can benefit from the R&D BER and thereby further increase compliance burden for companies. This proves particularly difficult for R&D efforts for basic research efforts and early-stage science, where the risk of anti-competitive effects is very low. As a reaction to corresponding demands from the legal community it was the Commission's expressed intention to make the application of the R&D BER easier. Any BER is meant to provide a safe harbour from the cartel prohibition after all without the need to conduct an in-dept individual assessment under Art 101(3) TFEU. It is thus an inherent requirement for any BER to provide clear and easy-to-applied rules. By introducing the concept of competition in innovation with the new assessment parameters, this goal cannot be achieved anymore and contracts the EU's own ambitions with this reform.

More specifically, the Commission introduces certain undefined terms for this assessment, for example that the necessary "R&D efforts" must be "competing" (this test is different to determining if products or technologies that are already in existence are competing) as well as "comparable", the third party must be "able and likely to independently engage" (Art 1(1) no. 18, no. 19 Draft R&D BER), and R&D pools must be "pursuing substantially the same aim or objective" (Art 1(1) no. 18 Draft R&D BER). In so far as the Draft Horizontal Guidelines address these terms (e.g. para. 146 et seq.), such guidance is not able to make up for the inherent uncertainty.

Also, for an R&D agreement between competitors in innovation to be group exempted the parties to the agreement must show that "three or more competing R&D efforts" exist (Art 6(3) Draft R&D BER). The burden of proof for the group exemption is thus on the parties. It is however not clear how the parties are meant to know of the existence of such competing R&D efforts by third parties, including of other R&D poles, taking into account that such R&D efforts are regularly early stage and relate to more or less unknown activities of potentially unknown players on a regularly global scale, hence global innovation markets. In addition, R&D activities are generally business secrets by the companies, in particular in R&D focused industries where such type of business secrets largely contribute to the respective company's market value. In BRAK's view, making the R&D partners to identify other (namely at least 3) competition R&D efforts in order to benefit from the group exemption bears the risk of setting off investigations / innovation market research efforts by the parties that may be viewed by the Commission as illegal information exchange with third party competitors with respect to their ongoing R&D activities. This scenario resulting from a legislative reform is questionable. It should rather be part of any regulator/enforcer's duties not to introduce legislation from which market participants can only benefit (like in the case of a BER) if they are able to show what other competing market participants are doing or planning in the same or a similar R&D environment, in particular if this information qualifies as competitive sensitive information.

Before this background, BRAK does not consider the described "three competing R&D efforts"-test to be suitable as a requirement for the application of the future R&D BER and proposes that it should be deleted from Art 6 Draft R&D BER altogether.

Should the Commission nevertheless decide to keep Art 6(3) Draft R&D BER, BRAK takes the view that it would be sufficient that two other “competing R&D efforts” exist to ensure sufficient competition on any future product and technology markets.

3. Standardization development in an IPR context

3.1 General observations

The Draft Horizontal Guidelines contain several important additions to chapter 7 dealing with standardization agreements in an IPR context. They build on cases decided by the European Commission (Motorola and Samsung), and the seminal judgement of the European Court of Justice in Huawei/ZTE. Many of the additions are to be welcomed. But the Draft Horizontal Guidelines still fall short of addressing many important issues, including those identified notably in the European Commission's "Call for evidence for an impact assessment" regarding "Intellectual property - new framework for standard-essential patents" (Ares(2022)1076263 – 14/02/2022).

3.2 Standard development

The Draft Horizontal Guidelines in para 464 refer to standard developments as opposed to standard setting. We feel that this is a minor stylistic change which puts more emphasis on the process character of developing a standard. We have no objections to this.

3.3 Competitors or non-competitors?

Para 466 mentions that participants in standardization are not necessarily competitors and that "standard development can, however, in specific circumstances where competitors are involved, also give rise to restrictive aspects on competition…". This statement appears to suggest that a standard development to be problematic under Art 101 (1) it must be established that competitors are involved. This seems to be misleading and an unwanted effect. We suggest deleting the reference "where competitors are involved" in para 466.

3.4 Different business models and roles in standard development and licensing

Para 469 acknowledges that different patent owners are involved in standard development and licensing. Some patent owners do not engage in standard development and take their primary interest in licensing patents they have either developed or acquired from third parties. Then there are patent owners who actively engage in standard development. Finally, there are downstream-only undertakings that implement the patents that read on a standard. The additions in para 469 appear helpful in making clear what the different commercial interests may be that are involved in standard development and SEP-licensing.

3.5 Patent hold-up versus hold-out

Para 470 explains the concept of a patent hold-up and adds to this the reverse situation that an unwilling licensee may try to avoid licensing of patents, which is described as patent hold-out. We feel this addition is meaningful and provides balance to the section. In addition, the

Horizontal Guidelines should be explicit that access to a standard means that that licenses are available for any market participant, and that it is not up to the patent owner to pick and choose.

There is one important element in para 470 that warrants more analysis. Notably, the Draft Horizontal Guidelines explain that an anti-competitive effect may occur where patent holders refuse to license the necessary IPR or try to extract excess rents by way of discriminatory or excessive royalty fees.

By using this wording, the Draft Horizontal Guidelines seem to equate licensing on fair and reasonable terms with non-excessive licensing rates. Excess rents is a concept that fits neatly into the framework of application of Art 102; this is however far less clear under Art 101 where no abuse is required. The reference in the Draft Horizontal Guidelines in Note 26 to the European Court of Justice's judgement in United Brands (case 27/76) therefore seems to be the wrong legal precedent for reference under Art 101.

In cases where there is a FRAND commitment in order to make a standard development compatible with Art 101 (1) or to come within Art 101 (3), the absence of a restriction of competition or outweighing positive effects to the benefit of consumers are the decisive point of reference. The European Commission should therefore make clear what concept it applies when discussing the compatibility of standard development under Art 101. As rightly noted in the European Commission's "Call for evidence for an impact assessment" regarding "Intellectual property - new framework for standard-essential patents" (Ares(2022)1076263 – 14/02/2022), the horizontal guidelines have in the last decade not succeeded to prevent the European Commission from finding "(i) insufficient transparency and predictability" and "(ii) uncertainty about FRAND terms and conditions".

The European Commission should therefore in the Draft Horizontal Guidelines be much clearer in identifying what is required under Art 101 (1) in terms of "fairness and reasonableness", so that the access to a standard is unrestricted (and not only "non-excessive"), and what the consequences are under Art 101 (1) if a patent holder does not honor a FRAND commitment. The Draft Horizontal Guidelines lack any interpretation of the consequences under Art 101 (2) for the standard development organization or its members from a failure to provide licenses to third parties at FRAND terms. This should be changed.

3.6 Market characteristics

Para 474 acknowledges that it is important to consider the nature of the goods or services affected by the standard, and the real conditions of the functioning and the structure of the market regarding their actual or likely effect on competition. This is a reasonable addition.

3.7 Disclosure of patents

Para 483 envisages a disclosure of patent number of patent application number. This adds clarity for the standard development organization and for implementers. It does not rectify the problems for implementers, however, as long as no license offers have been made and no most restrictive licensing terms have been declared. This means that important information for cost calculation in the development and commercialization of products that implement the standard are not available. This issue is not addressed properly. The Draft Horizontal Guidelines leave out this important element. This should be changed.

3.8 Limited responsibility of standard development organizations

Para 485 contains the most problematic and arguably most complex aspect, namely that the European Commission does not want to hold the standard development organization responsible for compliance of its members with the commitments they have given in order to bring the standard development in line with Art 101. It seems conceptually flawed, however, if the Draft Horizontal Guidelines establish quite detailed requirements that undertakings and organizations which engage in standard development need to fulfil without addressing the consequences if these requirements are not implemented properly in practice. According to the current draft guidelines, it suffices to give a FRAND commitment to bring the standard development in line with Art 101, and this is allegedly not called into question if the FRAND commitment is not honored later. This is not convincing. In many other areas of the application of Art 101 it does make a difference what effects are felt on the market, i.e. what undertakings do, and not what they say they would do. This is because Art 101 contains a reference to the object or the effect of an undertaking's behavior on the market. The European Commission should therefore address the question explicitly, including the application of Art 101 (2) in this context.

3.9 Determination of FRAND licensing terms

Para 486 makes a contradiction currently contained in the Draft Horizontal Guidelines very clear: According to the Draft Horizontal Guidelines, "the assessment of whether fees charged for access to IPR in the standard development context are unfair or unreasonable should be based on whether the fees bare reasonable relationship to the economic value of the IPR. The economic value of the IPR could be based on the present value added of the covered IPR and should be irrespective of the market success of the products which is unrelated to the patented technology." This appears a very sensible approach to determining the fee level, which is rooted in economics and aims to exclude market power effects. Para 487 also correctly mentions that the guidelines do not seek to provide an exhaustive list of appropriate methods to assess whether the royalty fees are excessive or discriminatory under Art 102.

By contrast, and here the contradiction becomes apparent, para 484 makes the equation that "FRAND commitments can prevent IPR holders from making the implementation of a standard difficult by refusing to license or by requesting unfair or unreasonable fees (<u>in other words excessive fees</u>) after the industry has been locked-in to the standard or by charging discriminatory royalty fees" (emphasis added). This passage is a reference to the European Court of Justice's judgement in Huawei/ZTE (C-170/13). This was an Art 102 case, however, not an Art 101 case.

By not being consistent regarding what is required for an antitrust compliant standard development under Art 101 (1) and its nexus to licensing terms that represent the "present value added of the covered IPR", "irrespective of the market success of a product which is unrelated to the patent technology" (para 486), the Draft Horizontal Guidelines miss the appropriate standard of reference when they apply wording from Art 102 cases (excessive) in para 470, 484, or 491. The guidelines should be more cautious and conscious of the difference between an unrestricted access (Art 101) and an excess rent standard (Art 102).

3.10 The development of a standard

Paras 493 et seq. contain meaningful additions to the general participation in standard development. In cases involving IPR and the development of technology standards, however, they fall short of the required rules and procedures that are necessary to address the problems identified by the European Commission in its "Call for evidence for an impact assessment" regarding "Intellectual property - new framework for standard-essential patents" (Ares(2022)1076263 – 14/02/2022). In this document (p. 2-3), the European Commission notes (quote, footnotes omitted):

> *"SEP licensing suffers from a <u>lack of transparency</u>. Some SDOs allow 'blanket' declarations which do not specify the patents that could be essential for a given standard. Other SDOs, such as the ETSI, require patent data from anyone contributing an SEP, but once a declaration is made by the SEP contributor, it is seldom updated. <u>As a result, it may not be clear who owns which SEP, whether declared patents are still essential, and which SEP is essential for which part of the standard</u>. Declarations to SDOs by those contributing an SEP only express the declarant's belief at the time of declaration that a patent may be or may become essential for the standard. <u>There is no 'quality control' by independent third parties</u>, unless the patents in question are examined in litigation or by a person assigned by a patent pool. According to some experts, only about 25-40% of all declared SEPs are truly essential for a given standard.*
>
> *SEP licensing also suffers from a <u>lack of predictability</u>. At the time the standard is adopted, SEP holders may not be aware of all potential applications of the standard. Therefore, <u>SEP holders usually wait for the market to develop before asking implementers to take a licence. This means that when products are developed and launched on markets, implementers may not have sufficient information as to which – and whose – patents they need to licence and what the royalty fees for this would be</u>.*
>
> *There is also another problem: current business practices mean that <u>coherent and meaningful information on FRAND licensing terms and conditions is usually not made publicly availabl</u>e. Both SEP holders and SEP implementers tend to keep confidential the results of their negotiations and agreed licensing terms and conditions – including FRAND royalties. This means that implementers, including start-ups and SMEs, <u>may not be able to factor licensing costs into their business models</u>. It also means that licensors may have a hard time forecasting and collecting revenue." (emphasis added)*

These are important issues, and it seems very unlikely that they can be properly addressed in a case-by-case approach under Art 102. The results of the European Commission's consultation on SEP-licensing should therefore be included in the Draft Horizontal Guidelines to arrive at a comprehensive set of rules and procedures to address the persisting problems in SEP-licensing, which are bad for inventors, patent owners, and implementers alike.